No. 17-1657

In the
Supreme Court of the United States

MISSION PRODUCT HOLDINGS, INC.,

Petitioner,

v.

TEMPNOLOGY, LLC, N/K/A OLD COLD LLC,

Respondent.

On Writ of Certiorari to the
United States Court of Appeals
for the First Circuit

BRIEF OF THE AMERICAN INTELLECTUAL PROPERTY LAW ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF NEITHER PARTY

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QUESTION PRESENTED

Whether, under § 365 of the Bankruptcy Code, a debtor-licensor's "rejection" of a license agreement—which "constitutes a breach of such contract," 11 U.S.C. § 365(g)—terminates rights of the licensee that would survive the licensor's breach under applicable non-bankruptcy law.

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STATEMENT OF INTEREST

The American Intellectual Property Law Association ("AIPLA"),[1] which files this brief with the written consent of both parties,[2] is a national bar association of approximately 13,500 members engaged in private and corporate practice, government service, and academia. AIPLA's members represent a diverse spectrum of individuals, companies, and institutions involved directly or indirectly in the practice of patent, trademark, copyright, and unfair competition law, as well as other fields of law affecting intellectual property. Our members represent both owners and users of intellectual property. AIPLA's mission includes providing courts with objective analyses to promote an intellectual property system that stimulates and rewards invention, creativity, and investment while

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[1] In accordance with Supreme Court Rule 37.6, AIPLA states that this brief was not authored, in whole or in part, by counsel to a party, and that no monetary contribution to the preparation or submission of this brief was made by any person or entity other than AIPLA and its counsel. Specifically, after reasonable investigation, AIPLA believes that (i) no member of its Board or Amicus Committee who voted to file this brief, or any attorney in the law firm or corporation of such a member, represents a party to the litigation in this matter; (ii) no representative of any party to this litigation participated in the authorship of this brief; and (iii) no one other than AIPLA, or its members who authored this brief and their law firms or employers, made a monetary contribution to the preparation or submission of this brief.

[2] AIPLA has obtained the consent of the parties to file this amicus brief, pursuant to Supreme Court Rule 37.3(a). Petitioner consented by counsel in a December 5, 2018 email sent to AIPLA. Respondent consented by counsel in a December 10, 2018 sent to AIPLA.

accommodating the public's interest in healthy competition, reasonable costs, and basic fairness. AIPLA has no stake in any of the parties to this litigation or in the result of this case. AIPLA's only interest is in seeking correct and consistent interpretation of the law as it relates to intellectual property issues.

SUMMARY OF ARGUMENT

The simple answer to the question presented is "no": rejection of a trademark license agreement does not terminate rights of the licensee that would survive the licensor's breach under applicable non-bankruptcy law.

The question presented assumes the rights of the licensee survive under applicable non-bankruptcy law. AIPLA posits that should be the test. Whether or not a trademark licensee retains its rights to use the licensed mark following the debtor-licensor's rejection of an executory contract containing a trademark license must be determined under applicable non-bankruptcy law. The resolution of that inquiry also should turn on the language of the contract (including any equitable relief that would otherwise apply to the license under applicable non-bankruptcy law).

A plain reading of Section 365 supports this position. Rejection by the debtor of an executory contract constituting a trademark license is only a breach. In the absence of the Bankruptcy Code specifically addressing trademark licenses, the effect of the breach must be decided under applicable non-bankruptcy law and the language of the contract.

This approach does not mean rights of a trademark licensee always survive rejection or that Section 365(n) of the Bankruptcy Code protects the rights of a trademark licensee. Nor does this approach mean the rights of a trademark licensee are always terminated following rejection, the view of the court of appeals in this case.

The rationale relied upon by the court of appeals in holding that the rights of the licensee were terminated following rejection was based upon the concept of the debtor-licensor's obligation to monitor quality control over the licensee. If the debtor-licensor failed to exercise quality control, a "naked license" could result, jeopardizing the continued validity of the debtor-licensor's trademark. *In re Tempnology, LLC*, 879 F.3d 389, 402–03 (1st Cir.), *cert. granted in part sub nom. Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 397 (2018). The court of appeals observed that the licensee's continued use of the licensed mark following rejection would force the debtor-licensor to choose between performing executory obligations of quality control or risk losing the trademark. *Id.* at 403.

AIPLA submits that a trademark licensor's obligation to control the quality of the goods associated with the licensed mark is not an obligation arising under the rejected trademark license, which, in some cases, may not even expressly address the issue. Rather, quality control is an independent obligation firmly grounded in trademark law. Following rejection, trademark law, not the rejected contract, continues to impose upon a debtor-licensor the obligation to

control the quality of the goods produced by its licensee if the licensor wishes to maintain the strength and value of the mark and retain rights to it. Consequently, although a *licensee* must *comply* with any quality-control provisions in the license as a matter of contract law, the complete failure of a *licensor* to *enforce* those provisions ordinarily will not constitute a breach of contract; instead, the potential negative consequence of that failure, namely, the risk of a naked license, has a different provenance.

The consequences of the debtor-licensor failing to enforce the quality-control provisions of a license following rejection are thus independent of the terms of the rejected contract. Rejection only relieves a debtor of executory obligations in the contract. Nothing in the Bankruptcy Code negates applicable trademark law following rejection of a trademark license.

AIPLA therefore urges the Court to limit its decision here solely to the question presented. Lower courts should be allowed to develop appropriate relief as to the rights of a trademark licensee following rejection on a case-by-case basis based upon the terms of the rejected contract and applicable non-bankruptcy law. Such a decision would be consistent with the legislative history of Section 365(n). AIPLA does not take a position on the ultimate issue of whether the rejection of the particular license at issue in this case should have resulted in termination of the licensee's rights. Its position is that the rejection of that license does not compel such a conclusion. The resolution of that issue depends on the terms of the specific license agreement and applicable non-bankruptcy law.

ARGUMENT

I. BACKGROUND

The test for trademark infringement under the common law and the federal Lanham Act is whether a defendant's conduct has created a likelihood of confusion as to whether its goods or services originate with the plaintiff or are otherwise connected to, affiliated with, or sponsored by the plaintiff. 15 U.S.C. §§ 1114(1), 1125(a). In effect, a trademark license is permission from the trademark owner to engage in behavior that would otherwise infringe the mark. *See Brennan's Inc. v. Dickie Brennan & Co.*, 376 F.3d 356, 364 (5th Cir. 2004) ("A license gives one party the right to use another party's mark (*i.e.*, to engage in otherwise infringing activity), generally in exchange for a royalty or other payment.").

Trademark licenses exist in myriad relationships and transactions. For example, the license may be straightforward permission to manufacture goods and apply the trademark owner's mark to the goods and to sell them. The license may describe a co-branding relationship, where two parties' marks are used on the same product, such as a component or ingredient used in a product offered by another, like an HP computer with a label "Intel Inside," indicating the brand of computer chip in the laptop. A trademark owner can license its mark for use on promotional goods, allowing a manufacturer of T-shirts to affix the mark to the front of the shirts. The T-shirt company might sell these shirts to the public and pay a per-product royalty to the trademark owner, or it might sell the shirts exclusively to the trademark owner for

its own distribution, with the trademark owner paying the licensee for the manufacturing. A trademark license may allow another to promote a sponsorship relationship such as, for example, where companies pay to become "platinum," "gold" and "silver" sponsors of a trade conference. A license to use a certification mark, such as the UL-branding on electrical goods, indicates the licensed party's goods meet the certifying party's standards.

There may be only one licensee or there may be many. The license can be exclusive or non-exclusive. Licensees can be divided territorially, as is often done in licenses for franchises. These licenses may vary with differing standards for different markets, such as a license one manufacturer to produce goods of one quality for the discount apparel channel and a license to a different manufacturer to produce a higher quality good for the department store apparel channel.

A license may be royalty-free if, for example, the promotional value of merely being identified with the licensee is adequate consideration. The payment can flow either way: trademark owners sometimes pay significant sums to licensees for their branding to appear in sporting venues and films.

Trademark licenses also come in many forms. A trademark license can be oral. *See, e.g., Transgo Inc. v. Ajac Transmission Parts Corp.*, 768 F.2d 1001, 1018 (9th Cir. 1985). It may be incomplete or ambiguous. *See, e.g., Intersport, Inc. v. Nat'l Collegiate Athletic Ass'n*, 885 N.E.2d 532, 541 (Ill. Ct. App. 2008) (referring to dictionary definitions to resolve meaning of disputed term in license). It may only be implied,

based on how the parties interacted. *See, e.g., Villanova Univ. v. Villanova Alumni Educ. Found., Inc.*, 123 F. Supp. 2d 293, 308 (E.D. Pa. 2000).

This complexity and variety make it difficult to agree on simple rules for how to treat trademark licenses in bankruptcy. In fact, the legislative history of the enactment of Section 365(n) plainly states that Congress recognized trademarks were unique and, because it required more study, expressly postponed congressional action in this area to allow bankruptcy courts to develop an equitable treatment for trademark licenses. S. Rep. No. 100-505, at 5 (1988).

The omission of trademarks from the definition of intellectual property in Section 365(n) was thus intentional. The decision by the court of appeals that Section 365 never allows for an election by the licensee to retain a license granted in a rejected contract is wrong because such an interpretation will always favor the licensor and frustrates the intent of Congress. It cannot be considered an equitable treatment, and it precludes any further consideration of what might be such a treatment.

Treating the rejection of an executory contract granting a trademark license as merely a breach is the most reasonable interpretation of the statute. With a directive to apply non-bankruptcy law from this Court, bankruptcy courts may apply and, as necessary, further develop that law to reach equitable treatments of trademark licenses in bankruptcy. This is not to say that bankruptcy courts may resort to "undefined considerations of equity" in determining the effect of rejection in a particular case. *Butner v.*

United States, 440 U.S. 48, 56 (1979). Rather, the bankruptcy court's treatment of a breached trademark license should rest on applicable non-bankruptcy law, including, where appropriate, recognized equitable doctrines that would be available had the breach occurred outside of bankruptcy.

II. THE SIGNIFICANCE OF REJECTION OF TRADEMARK LICENSES UNDER SECTION 365

A. Section 365 of the Bankruptcy Code Does Not Mandate Termination of a Trademark License Upon Rejection of the Contract

1. Rejection Under Section 365 Results in a Breach, and Applicable Non-Bankruptcy Law Determines the Parties' Rights

Section 365(a) of the Bankruptcy Code allows a bankruptcy trustee or debtor-in-possession (collectively referred to herein as a debtor) either to assume an executory contract and continue to satisfy all of its contractual obligations or to reject the contract and be relieved of the obligation to specifically perform any of its affirmative obligations under the contract. 11 U.S.C. § 365(a).[3]

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[3] AIPLA notes this litigation involves only executory trademark licenses, not trademark licenses determined to be nonexecutory. *See, e.g., In re Interstate Bakeries Corp.*, 751 F.3d 955 (8th Cir.

Should the debtor reject an executory contract, section 365(g) of the Bankruptcy Code expressly provides that such rejection "constitutes a breach of such contract ... immediately before the date of the filing of the petition." 11 U.S.C. § 365(g). Absent a specific provision of the Bankruptcy Code to the contrary, the consequences of that breach on the counterparty's rights under the contract are properly determined by the terms of the contract and applicable non-bankruptcy law. The Bankruptcy Code contains no such specific provision for rejection of a trademark license.[4]

In 1985, prior to the Bankruptcy Code containing any specific provision as to the effect of rejection of an intellectual property license, the Court of Appeals for the Fourth Circuit nevertheless concluded that, as a matter of bankruptcy law, a debtor-licensor's rejection of an intellectual property license terminated the non-debtor-licensee's rights to use the previously licensed intellectual property. *Lubrizol Enters. v. Richmond Metal Finishers, Inc.*, 756 F.2d 1043 (4th Cir. 1985). The decision was controversial and heavily criticized. In 1988, Congress directly responded to *Lubrizol* by enacting section 365(n) of the

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2014) (en banc); *In re Exide Techs.*, 607 F.3d 957 (3d Cir. 2010), *as amended* (June 24, 2010).

[4] The Bankruptcy Code does contain specific provisions for the rejection of other types of contracts, such as section 365(h) addressing the rejection of an unexpired lease of real property and as discussed herein, addressing the rejection of certain types of intellectual property contracts but not contracts containing a trademark license.

Bankruptcy Code, which provides that, upon the rejection of an intellectual property license in a debtor-licensor's bankruptcy case, the non-debtor licensee has the option of treating the license as terminated or continuing to use the licensed intellectual property while making applicable royalty payments for the duration of the license's term without setoff and without claiming an administrative expenses for damages resulting from the breach.[5]

While section 365(n) of the Bankruptcy Code addressed "intellectual property" licenses, Congress specifically chose not to include trademarks in the definition of "intellectual property" found in section 101(35A) of the Bankruptcy Code. 11 U.S.C. §§ 101(35A), 365(n). The exclusion of trademarks was not a glaring oversight, but an intentional omission:

> [T]he bill does not address the rejection of executory trademark, trade name or service mark licenses by debtor-licensors. While such rejection is of concern because of the interpretation of section 365 by the Lubrizol court and others, ... such contracts raise issues beyond the scope of this legislation. In particular, trademark, trade name and service mark licens-

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[5] An "administrative expense" claim must be paid in full on the effective date of a confirmed chapter 11 plan. 11 U.S.C. §§ 503(b)(1), 507(a)(2), 1129(a)(9)(A). *See, e.g., Reading Co. v. Brown*, 391 U.S. 471 (1968) (decided under Bankruptcy Act, trustee's actions can create an administrative expense claim against the estate).

> ing relationships depend to a large extent on control of the quality of the products or services sold by the licensee. Since these matters could not be addressed without more extensive study, it was determined to postpone congressional action in this area to allow the development of equitable treatment of this situation by bankruptcy courts.

S. Rep. No. 100-505, at 5 (1988). As is evident from the legislative history of section 365(n), the exclusion of trademarks from its ambit was not an endorsement of the *Lubrizol* approach regarding the effect of the rejection of a trademark license in a licensor's bankruptcy case.

In *Sunbeam Products, Inc. v. Chi. American Manufacturing, LLC*, 686 F.3d 372 (7th Cir. 2012), the Court of Appeals for the Seventh Circuit declined to follow the *Lubrizol* approach in determining the effect of rejection of a trademark license agreement in a licensor's bankruptcy case. It held instead that the rejection of a trademark license agreement in a licensor's bankruptcy case constitutes, under section 365(g) of the Bankruptcy Code, a breach of such executory contract by the licensor. Outside of bankruptcy, such a breach would not, *in and of itself*, terminate the licensee's right to continue to use the licensed mark(s) or its obligation to comply with the license, if it elected to continue to use the mark. *Id.* at 377.

The First Circuit Bankruptcy Appellate Panel in this case agreed with the *Sunbeam* rationale. As articulated by the bankruptcy appellate panel:

> Applying *Sunbeam*'s rationale, we conclude that, while the Debtor's trademark and logo were not encompassed in the categories of intellectual property entitled to special protections under § 365(n), the Debtor's rejection of the Agreement did not vaporize Mission's trademark rights under the Agreement. Whatever post-rejection rights Mission retained in the Debtor's trademark and logo are governed by the terms of the Agreement and applicable non-bankruptcy law.

Mission Prod. Holdings, Inc. v. Tempnology LLC (In re Tempnology LLC), 559 B.R. 809, 822-23 (1st Cir. B.A.P. 2016).

In reversing the decision of the bankruptcy appellate panel, the Court of Appeals for the First Circuit rejected the conclusion in the *Sunbeam* case and held that bankruptcy extinguishes a trademark licensee's right to continue to use a licensed mark when a trademark license agreement is rejected in the licensor's bankruptcy case. The court concluded that Section 365 of the Bankruptcy Code is intended to empower a bankrupt debtor to free itself from burdensome performance obligations under an executory contract and that a licensee's continued use of licensed marks on a post-rejection basis would frustrate that purpose. 879 F.3d at 404.

In doing so, the court of appeals properly recognized that a trademark licensor must maintain some measure of control over the quality of goods associated with the licensed mark or risk the loss of its rights in that mark under the doctrine of abandonment. *Id.* at 402-03. Ignoring the trademark-law provenance of that obligation, however, the court treated it as an executory obligation of the debtor and concluded that the alleviation of that obligation required a holding that rejection extinguishes a licensee's right to continue using any marks covered by the license. *Id.* at 404.

As discussed in more detail in the following section, any burden attending the maintenance of quality control is not contractual and does not arise under the rejected contract, but rather is an inherent obligation of a trademark owner originating in trademark law. Indeed, as quoted by the court of appeals, the contract in question contained a "right" to monitor quality control, not an obligation to do so. *Id.* at 402 ("The Agreement provides that Debtor 'shall have the right to review and approve all uses of its Marks,' except for certain pre-approved uses.").

While rejection of an executory contract converts the debtor's "unfulfilled obligations" to the counterparty under the contract into damages and insulates the debtor from specific performance of affirmative obligations imposed by the contract, rejection does not alter applicable trademark law following a licensor's breach. Rejection of a trademark license alters neither the debtor-licensor's independent quality-control obligation under trademark law nor the

parties' remedies should the debtor-licensor fail to fulfill that obligation following rejection. Rejection does not vaporize the rights of the counterparty to such a contract, *Sunbeam Prods.*, 686 F.3d at 377, nor does rejection vaporize applicable trademark law following rejection. Nothing in the Bankruptcy Code relieves a debtor-licensor of the effect of trademark law following the rejection of a trademark license.

The bankruptcy appellate panel persuasively concluded in this case that, as a matter of bankruptcy law, rejection did not extinguish the licensee's right to use the licensed marks and that the terms of the agreement and applicable non-bankruptcy law govern the rejection's effect on the agreement. *Tempnology*, 559 B.R. at 822-23. In the absence of a provision of the Bankruptcy Code specifically addressing the effect of the rejection of a trademark license, the holding of the bankruptcy appellate panel properly construes the Bankruptcy Code in its current form. *Butner*, 440 U.S. at 55 (holding that the justification for application of state law in a bankruptcy context to define property interests is not limited to ownership interests). This Court should reach the same conclusion.

2. The Need to Exercise Control Over a Trademark Licensee Arises Independently Under Trademark Law and Does Not Amount to a Debtor-Licensor Performing Under an Otherwise Rejected Contract

Subject to certain exceptions not relevant here, the rights to a particular trademark under United

States law depend on the ongoing use of the mark. That use need not be by the mark's owner itself. Rather, both the common law and Section 5 of the Lanham Act, 15 U.S.C. § 1055, permit the owner to allow another party, a "related company," to use the mark. *See, e.g., Turner v. H M H Publ'g Co.*, 380 F.2d 224 (5th Cir. 1967) ("Section 5 of the Lanham Act ... contemplates that a trade or service mark may be acquired through its use by controlled licensees, even though the registrant itself may not have used the mark."). The use by that "related company, i.e., a licensee, will inure to the licensor's benefit if the licensor has controlled the licensee's use of the mark. 15 U.S.C. § 1127 (defining "related company" in terms of control).

Section 45 of the Lanham Act provides that a trademark will be abandoned if it loses significance as an indication of origin of the mark owner's goods. *Id.* This may happen if the licensor has not exercised control over the nature and quality of its licensee's goods and services. In such a case, the licensee's use does not inure to the licensor's benefit, and the mark will begin to indicate that the goods associated with the mark originate with the licensee, rather than the licensor. In extreme cases, the mark may lose all significance as a trademark.

At that point, the parties' agreement will become a "naked" license that may work a forfeiture of the licensor's rights. *See generally Sheila's Shine Prods., Inc. v. Sheila Shine, Inc.*, 486 F.2d 114, 123-24 (5th Cir. 1973); *Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 366 (2d Cir. 1959). Whether

abandonment actually occurs is a fact-specific inquiry, and the legal standards for finding a naked license vary among the various courts of appeal. *See, e.g.*, *Patsy's Italian Rest., Inc. v. Banas*, 658 F.3d 254, 264 (2d Cir. 2011) ("Although some forms of trademark abandonment may result in a loss of all rights in the mark, abandonment of a mark through naked licensing has different effects on the validity of the mark in different markets." (citation omitted)); *Sheila's Shine*, 486 F.2d at 125 ("[A] trademark owner has an appropriate time, or grace period, for the exercise of control over a licensee's use of a mark. Of necessity, this period varies according to the peculiar facts of each individual case.").

Because of the common-law and statutory origins of the control requirement, a trademark license typically does not discuss quality control as an affirmative duty of the licensor, but instead defines the required quality in terms of the compliance obligations of the licensee. The licensee's obligation to comply with the quality-control provisions of the license is contractual in nature. In a properly drafted license, therefore, the licensor's remedy for the licensee's failure to comply with those terms is termination of the license.

In contrast, the licensor's quality-control obligation arises under applicable non-bankruptcy law because of the debtor-licensor's decision to enter into a trademark license and is a natural consequence of that decision. Allowing a licensee to retain its license after rejection therefore should not require a debtor to perform an executory license agreement or impose a new obligation on the debtor-licensor. Whether or not

it rejects the license, a debtor-licensor is not relieved of the obligation created under trademark law to preserve the licensed mark's origin-indicating significance if the debtor-licensor wishes to maintain the mark as an asset.

The maintenance of quality control therefore is an important obligation of all trademark licensors, but the court of appeals in this case may have overstated the burden of that obligation. Specifically, a licensor need not require a particular level of quality so long as it has the ability to enforce whatever level of quality it sets. "'[Q]uality control' does not necessarily mean that the licensed goods or services must be of 'high' quality, but merely of equal quality, whether that quality is high, low or middle." *Barcamerica Int'l USA Tr. v. Tyfield Imps., Inc.*, 289 F.3d 589, 598 (9th Cir. 2002). In other words, control, not the actual quality subject to that control, is the issue in the inquiry into whether a naked license exists.

Although a trademark licensor may wish to escape a license for myriad reasons, two in particular merit consideration in this proceeding. First, the licensor may conclude that the investment required for the continued monitoring of a licensee's compliance with a particular quality-control provision recited in the license is no longer cost-effective. Second, the licensor's goal may be to monetize its mark to the fullest extent possible by securing higher royalty payments from a different licensee; of course, any claimed burden associated with quality control is merely a pretext in this context.

Whether in or out of bankruptcy, a licensor genuinely motivated by the first of these considerations can approach its licensee and propose an amendment to the license to eliminate the quality-control provision at issue. Because such an amendment will work exclusively in the licensee's favor, the licensee ordinarily can be expected to accept it. Even if the licensee does not do so, however, or if the licensor prefers not to raise the issue, the licensor can simply elect not to enforce the objectionable provision, so long as it continues to assure a minimum level of quality in some way. Such a strategy can result in the licensor's waiver of the provision on a going-forward basis and a diminishment in the quality of the goods sold under the license. Even if it occurs, that diminishment will not itself render the license a naked one because whether a good produced under the license is "objectively 'good' or 'bad' is simply irrelevant." *Id.* Trademark licensors in bankruptcy proceedings therefore have an option short of rejection, one that does not expose licensees to an outright rejection motivated by the licensor's desire for better terms from another licensee.

Of course, if the debtor-licensor fails to fulfill its quality-control obligation altogether following rejection, a clever licensee could try to take advantage of the situation by electing to retain the license following rejection and then arguing the debtor-licensor has abandoned the mark by failure to exercise control. Nevertheless, licensee estoppel can ameliorate this risk. As a general rule, a trademark licensee is estopped from challenging the validity of the licensor's title because the licensee has recognized the validity of the licensor's ownership by agreeing to the license.

See, e.g., John C. Flood of Va., Inc. v. John C. Flood, Inc., 642 F.3d 1105, 1110 (D.C. Cir. 2011); *Seven–Up Bottling Co. v. Seven–Up Co.*, 561 F.2d 1275, 1279–80 (8th Cir. 1977). *But see Idaho Potato Comm'n v. M & M Produce Farm & Sales*, 335 F.3d 130, 137 (2d Cir. 2003) (invoking public interest to reject licensee estoppel provision in certification mark license).

B. Applying Non-Bankruptcy Law to Determine the Effect of Breach Will Allow Courts to Develop Equitable Treatment of Trademark Licenses in Bankruptcy

Although AIPLA rejects the *per se* rule applied by the court of appeals in this case that trademark licenses must always terminate when the underlying contract is rejected, it cautions against an assumption that trademark licenses always survive or that the licensee will be free to fully enjoy the license following rejection. Outside of bankruptcy proceedings, the proper treatment of a licensor's breach of a trademark license turns on the express terms of the license and governing state and federal law. Whether a licensee may elect not to terminate the contract, and the relief available to the parties in bankruptcy, depends on the contract and applicable non-bankruptcy law, subject to the unavailability of specific performance against the debtor-licensor following rejection.

Furthermore, perhaps more so than in any other area of intellectual property law, there is a strong public interest component in trademark law.

The terms of the license and governing state and federal law should guide the bankruptcy court's actions when it fashions relief following rejection.

1. Non-Bankruptcy Law Will Govern the Licensee's Continued Use of the Licensed Mark After Rejection

If a license is not terminated, and the licensee elects to continue using the licensed mark under the rejected license, it must continue to fulfill its obligations to the licensor:

> Under basic contract principles, when one party to a contract feels that the other contracting party has breached its agreement, the non-breaching party may either stop performance and assume the contract is avoided, or continue its performance and sue for damages. Under no circumstances may the non-breaching party stop performance and continue to take advantage of the contract's benefits.

S & R Corp. v. Jiffy Lube Int'l, Inc., 968 F.2d 371, 376 (3d Cir. 1992).

A failure of a licensee to adhere to the terms of the rejected license, including the licensor's standards, also means the resulting goods are unlicensed. Continued use of the licensor's trademark on them infringes that mark, potentially exposing the licensee to infringement remedies. *See, e.g., El Greco Leather Prods. Co. v. Shoe World, Inc.*, 806 F.2d 392, 395 (2d

Cir. 1986) (failure to obtain certificate of inspection from licensor rendered mark on goods infringing); *see also Warner-Lambert Co. v. Northside Dev. Corp.*, 86 F.3d 3, 8 (2d Cir. 1996) (enjoining the sale of stale product even though the contract did not expressly prohibit its sale).

Admittedly, not all licensing situations may be as straightforward as reading a written agreement and simply enforcing those terms not requiring specific performance by the licensor. Sometimes trademark licenses are informal, incomplete, or ambiguous; indeed, they may not be written. *See, e.g.*, *Transgo*, 768 F.2d at 1018 (describing oral license). The bankruptcy court may therefore need to determine exactly what the contract requires of the licensee. Nevertheless, any such need will not be extraordinary and does not justify terminating licenses to reduce the burden associated with administering the estate. There is ample precedent to decide any issues that may arise.

A licensee's duty to comply with its quality control obligations can take many forms. The licensee's duty can be described expressly in a contract, to a greater or lesser degree, and may be expressed briefly and without detail:

> The use by each of the other's Marks shall be in accordance with the standards for quality control set by the owner of the Marks, and solely for the purposes permitted by this Agreement, and subject to the other party's right to review and approve

> (or reject) in advance each proposed use by the first party of the other party's Marks.

3 MARY M. SQUYRES AND NANETTE NORTON, TRADEMARK PRACTICE THROUGHOUT THE WORLD, JOINT PROMOTION AND MARKETING AGREEMENT Appendix 30(B) (April 2018 update). Or the licensor may have set out for the licensee standards in detail, describing the right to approve style, colors, materials, method of fabrication and labeling, and prohibiting the use of noxious chemicals in manufacture. *See, e.g., Trademark License Agreement Between Tommy Bahama Group, Inc. and Phoenix Footwear Group, Inc.* (Dec. 8, 2008) https://www.sec.gov/Archives/edgar/data/26820/000119312508253523/dex101.htm.

If not in the agreement itself, quality control may be manifested in the actual control exercised by a licensor. *See, e.g., Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 367 (2d Cir. 1959) (control adequate when local sales representatives visited store). There can also be adequate control if the relationship is one allowing the court to assume the licensee is acting in the best interest of the licensor. *See, e.g., Taco Cabana Int'l, Inc. v. Two Pesos, Inc.*, 932 F.2d 1113, 1121-22 (5th Cir. 1991) (finding that two brothers who ran a chain of restaurants and later divided the business could rely on each other to maintain quality), *aff'd* 505 U.S. 763 (1992); *Transgo*, 768 F.2d at 1017-18 (finding sufficient control where licensor was a friend of licensee, licensee was knowledgeable about the goods, and only a small amount of product was manufactured by licensee); *Land O'Lakes Creameries, Inc. v. Oconomowoc Canning Co.*, 330

F.2d 667, 670 (7th Cir. 1964) (finding sufficient control where the licensee sold product for 40 years without complaints about quality).

No matter how it is done, control is the sine qua non of a trademark license. *See generally* F. Vern Lahart, *Control—The Sine Qua Non of a Valid Trademark License*, 50 TRADEMARK REP. 103 (1960); *see also Taco Cabana*, 932 F.2d at 1121 ("The purpose of the quality-control requirement is to prevent the public deception that would ensue from variant quality standards under the same mark or dress."). Whether or not the license says anything about how the control is exercised, it is "the principal requirement applicable to all trademark licenses." *E. & J. Gallo Winery v. Gallo Cattle Co.*, 967 F.2d 1280, 1290 (8th Cir. 1992). Therefore, in construing a license, the only appropriate construction is confirming the licensee's duty to observe the licensor's standards.

Furthermore, if the licensee cannot produce or sell the goods or services under the trademark by reason of quality-control provisions, the effect would be that the licensee could no longer enjoy the benefit of the license. The licensee presumably would have no choice but to terminate the contract. Consider as an example a contract containing a trademark license. The contract requires the licensee to submit a prototype for a product to the licensor for approval before manufacture can begin and, if the licensor fails to respond within a set period, the prototype will be rejected, preventing the product's manufacture. If the licensor does not respond, the licensee may not manufacture the product and, if the license so provides, is left only with a claim against the licensor for breach.

As another example, suppose a trademark license allows the licensee to manufacture a bottled beverage by adding carbonation and water to a proprietary syrup provided by the licensor, using the trademark on the bottled product. Assume further the license does not have any express quality control provisions, stating only how much syrup the licensee must purchase and requiring that it be diluted and carbonated by a certain amount. Even in the absence of an express quality control provision, the end product, the bottled drink, will be of known quality assured by the use of the proprietary syrup. If the licensor no longer manufactures syrup, it must be clear the licensee cannot substitute a different syrup, even if the agreement is silent, because the use of the proprietary syrup is fundamental to ensuring the licensed product meets the licensor's quality control standards.

A bankruptcy court would have the authority to clarify the contract in this manner and forbid the licensee from using a different syrup. If it means the licensee can no longer create bottled drinks, the licensee's only remedy is monetary relief for the licensor's breach in failing to provide the syrup. The licensee does not have the latitude to create an altogether different drink with a different syrup and then sell it under the formerly licensed mark. Even though the bankruptcy court may make such a determination, the ruling is not based on bankruptcy law, rather the ruling is based on non-bankruptcy law applicable to the license in question and the Code's provision prohibiting specific performance against the debtor.

Where terms are ambiguous or missing courts have implied them. For example, the term of the license may be unclear. *See, e.g., TMT N. Am., Inc. v. Magic Touch GmbH*, 124 F.3d 876, 882 (7th Cir. 1997) (affirming magistrate judge's conclusion that the trademark was implicitly licensed for the term of the agreement); *Bank of N.C. v. RCR Mktg., LLC*, No. 1:10CV663, 2010 WL 5020502, at *4 (M.D.N.C. Dec. 3, 2010) (where there was no evidence of a written license, ordering licensee to comply with debtor-licensor's quality control). As with any contract, it is well within the bankruptcy court's ability and powers, guided by applicable non-bankruptcy law and relying on well-settled principles of contract interpretation, to ascertain the true meaning of these contracts, including the geographic and temporal scope of the license granted and the goods and services involved, the conditions on the grant of the license, and the responsibilities of the licensee.

2. Non-Bankruptcy Law Occasionally Allows for the Termination of a Trademark License in the Absence of a Breach by the Licensee

AIPLA believes it possible, without resorting to unenforceable *ipso facto* clauses, to structure transactions involving a trademark license so the license cannot or does not survive in the event of a licensor breach. Treating rejection as merely a breach will be consistent with the parties' expectations in these circumstances.

Furthermore, even in the absence of such a result, trademark law has long recognized that contracts regarding trademarks can be terminated in certain circumstances. A bankruptcy court may be able to invoke non-bankruptcy law principles to terminate or modify a license. This principle arises from this Court's decision in *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969). *Idaho Potato Comm'n*, 335 F.3d at 137 (citing *Lear* as the source of the law as applied in the trademark context); *Beer Nuts, Inc. v. King Nut Co.*, 477 F.2d 326, 328 (6th Cir. 1973) (same). *Lear*, a patent case, established that the public interest plays a role in determining the enforceability of provisions of a patent license. *Lear*, 395 U.S. at 670–71. Although originally stated in a patent case, this principle has also been applied to trademark licenses.

Trademark law, even more so than patent law, has a significant public interest component. The public is a stakeholder in trademark law, because the law protects consumers from being deceived into purchasing an unwanted good bearing an infringing mark, *Amoskeag Mfg. Co. v. D. Trainer & Sons*, 101 U.S. 51, 62 (1879). That law also ensures needed vocabulary is available. *Park 'N Fly, Inc. v. Dollar Park & Fly, Inc.*, 469 U.S. 189, 210 (1985). Although originally stated in a patent case, this principle has also been applied to trademark licenses.

Under applications of these principles in trademark cases, a party entering into an agreement with respect to a trademark will be held to its obligations unless enforcement of the contract would injure the public. *VISA Int'l Serv. Ass'n v. Bankcard Holders of Am.*, 784 F.2d 1472, 1473 (9th Cir. 1986) (considering

public interest in avoidance of confusion); *Beer Nuts, Inc. v. King Nut Co.*, 477 F.2d 326, 329 (6th Cir. 1973) (depletion of vocabulary); *Proriver, Inc. v. Red River Grill, LLC*, 83 F. Supp. 2d 42, 45 (D.D.C. 1999) (confusion); *Kegan v. Apple Comput., Inc.*, No. 95 C 1339, 1996 WL 667808, at *3 (N.D. Ill. Nov. 15, 1996) (vocabulary); *see also Peyrat v. L.N. Renault & Sons, Inc.*, 247 F. Supp. 1009, 1014 (S.D.N.Y. 1965) (an agreement between parties to a trademark controversy "is valid and enforceable so long as no injury is caused to the public").

A court should weigh the public interest and resulting harm against contract law's policy of holding parties to the terms of their agreements. *VISA Int'l*, 784 F.2d at 1474–75 (citing *T & T Mfg. Co. v. A.T. Cross Co.*, 449 F. Supp. 813, 827 (D.R.I.), *aff'd*, 587 F.2d 533 (1st Cir. 1978)); *Beer Nuts*, 477 F.2d at 328. If the public harm outweighs the policy of holding parties to their agreement, the agreement can be terminated or modified. *VISA Int'l*, 784 F.2d at 1473-74 (considering both rescission and modification of contract); *Idaho Potato Comm'n*, 335 F.3d at 139 (preventing enforcement of no-challenge provision in license agreement for certification mark). Thus, in certain situations, the debtor-licensor may have an opportunity to seek to rescind or modify the license if the license otherwise will harm the public interest.[6]

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[6] A debtor seeking such equitable relief following rejection may be required to seek such relief in an adversary proceeding. Fed. R. Bankr. Pro. 7001(7) (injunction or other equitable relief) and 7007(9) (declaratory relief).

III. CONCLUSION

Under bankruptcy law, the rejection of an executory contract constitutes a breach of the contract. Clarification that the effect of the breach and any available relief must be determined using recognized principles of non-bankruptcy law and applicable principles of equity, subject to limits imposed by the Bankruptcy Code on specific performance, will better enable bankruptcy courts to determine the parties' rights following rejection of a trademark license and serve the public interest in preventing consumer confusion.[7] In addition, parties negotiating trademark license agreements will be able to make better-informed decisions about the provisions that need to be included in such agreements to protect their respective interests in the event of a licensor bankruptcy.

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[7] This approach will not disadvantage less capitalized licensors in their negotiations with potential licensees. Potential licensees may perceive these licensors as more likely to seek bankruptcy protection than larger companies (and then reject licenses into which they have entered). These licensors therefore may have to make concessions in negotiations in light of the risk they will reject the licenses down the road. They also may miss out on licensing opportunities altogether because the risk of their possible bankruptcy is perceived to be too high. More certainty for the licensee means the small business licensor will have greater opportunity to enter into favorable licensing arrangements.

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